THE SMALL BUSINESS JOBS AND CREDIT ACT: A LEGAL AND ECONOMIC ANALYSIS OF THE STIMULUS BILL FROM BOTH A MICROECONOMIC AND MACROECONOMIC PERSPECTIVE

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I. INTRODUCTION

Faced with a floundering economic recovery, headlined by struggling small business owners, Congress passed the Small Business Jobs and Credit Act of 2010 ("Act") to address the ongoing effects of the financial crisis on small businesses. The Act provides the Secretary of the Treasury the means to make capital investments in lending institutions in order to increase the availability of credit for small businesses.[1] The law helps small businesses get the capital they require to operate successfully through increasing the availability of small business loans,[2] increasing their desirability to investors,[3] and offering them tax breaks.[4] However, there is much debate as to whether this Act is actually going to be of any significant benefit to small business owners, entrepreneurs or the economy in general.

Opponents of the new law feel that the measures taken to make credit available to small businesses will not be effective because the new law is redundant when coupled with the Troubled Asset Relief Program ("TARP"), which was effective in preventing an economic crash, but has not been nearly as successful in decreasing unemployment and easing the credit constraints on small businesses.[5] Critics argue that there is enough credit available to small businesses. The problem is that small businesses simply cannot justify taking out a loan without sales projections.[6] As a

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[1] Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.

[2] *Id.*

[3] *Id.* § 2011 (making investing in businesses more desirable by allowing for the tax exclusion of gains from investments in small businesses).

[4] *Id.* § 2011–14.

[5] W.W., *How effective was TARP, really?*, ECONOMIST, Oct. 8, 2010, http://www.economist.com/blogs/democracyinamerica/2010/10/public_opinion_and_bailouts.

[6] William C. Dunkleberg & Holly Wade, *NFIB Small Business Economic Trends*, NAT'L FED'N INDEP. BUS., (Jan. 2011), *available at* http://www.nfib.com/Portals/0/PDF/sbet/sbet201101.pdf.

result, many feel this law will be as ineffective in reducing unemployment and encouraging the profitability of small businesses as TARP.

In addition to the redundancy of the Act, the red tape and small window of opportunity to take advantage of the benefits created by the Act could make Congress' intentions inoperable for businesses in the real world. Despite Congress' best intentions, the Act will not create a meaningful change in the economic climate for small businesses because its focus on making credit available to small businesses is insufficient. The challenges facing small businesses are too complex and multifaceted to be solved by a one-dimensional, legislative approach. In addition to a credit crunch, entrepreneurs are struggling with an uncertain economic climate, significant changes in the healthcare system, and a lack of consumer demand for their products. The law will benefit small businesses by addressing the problem of credit availability, but the Act will only bide time and facilitate the firm's ability to persevere. The Act does not address any of the other problems small businesses are facing and, as a result, the Small Business Jobs and Credit Act will not have the desired macroeconomic effect Congress intended.

II. ANALYSIS OF THE SMALL BUSINESS JOBS AND CREDIT ACT

The Act was passed and signed by the President on September 23, 2010.[7] The Act was created by Congress to help spur job creation, which has remained stagnant despite economic recovery in other areas.[8] The bill was specifically designed to alleviate credit constraints and provide additional temporary tax benefits to small businesses in order to facilitate job growth.[9] The Act provides a multitude of opportunities for small business owners, ranging from access to credit by making loans available, tax breaks for small businesses, tax incentives for business activity, and even tax breaks for small business investors.[10]

The structure of the Act is broken down into two parts, each taking a different approach to addressing the credit shortage for small and entrepreneurial businesses. The primary function of the Act is the creation of the Small Business Lending Fund Program ("SBLFP").[11] The purpose behind this portion of the law is "to address the ongoing effects of the financial crisis on small businesses by providing temporary authority to the Secretary of the Treasury to make capital investments in eligible institutions

[7] Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.
[8] Justin Lahart, *Layoffs Ease, but Hiring Stagnant*, WALL ST. J., Oct. 8, 2010, at A2.
[9] Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.
[10] *Id.*
[11] *Id.* § 4101, 124 Stat. at 2582.

in order to increase the availability of credit for small businesses."[12] The SBLFP has a budget of $30 billion, which the Secretary of the Treasury loans to eligible lending institutions in exchange for shares of preferred stock or other similar assets.[13] Once disbursed, the loan money is incentivized to increase the amount of small business and entrepreneurial loans. The SBLFP sets the default interest rate or dividend at five percent for the first two years.[14] During the trial period, the Treasury keeps track of the financial information as well as the loan activity of the borrower through quarterly and yearly reports that must be filed in order to receive the loans.[15] Using these reports, the Treasury calculates the borrower's percent increase or decrease in small business or entrepreneurial lending. The percent change in small business lending determines the interest rate for the borrower in the next term; discounting the interest rate of those borrowers that increase their small business lending and increasing the rate for those who did not.[16] If the borrower increases their small business lending by less than 2.5%, the interest rate remains at five percent; for every additional 2.5% the borrower increases their small business lending, they receive an additional percent decrease on the loan's interest rate with a minimum interest rate of one percent.[17] The adjusted interest rate persists for the next two-and-a-half years. At the end of the adjusted rate period, the interest rate jumps to nine percent until the ten year term ends, five-and-a-half years later.[18] This serves as an incentive for the borrower to lend the money received from SBLFP to small or entrepreneurial businesses in order to receive a lower interest rate.[19] As a result, banks are able to make a larger profit on the SBLFP money they lend because of a larger spread between the interest received from the small business and the interest they owe to the United States Treasury.[20]

There are limits to the amount of loans applicants may receive. Eligible institutions with assets of $1 billion or less may only receive a capital investment from the SBLFP up to five percent of their risk-weighted assets. Institutions with assets of more than $1 billion may only borrow up to three percent of their risk weighted assets.[21]

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[12] *Id.*
[13] *Id.* § 4103, 124 Stat. at 2585.
[14] *Id.* § 4103(d)(5)(A)(i), 124 Stat. at 2588.
[15] *Id.* § 4103(d)(5)(B), 124 Stat. at 2589.
[16] *Id.* § 4103(d)(5)(A), 124 Stat. at 2588–89.
[17] *Id.* § 4103(d)(5)(A)(iii), 124 Stat. at 2589.
[18] *Id.*
[19] *Id.* This is due to the reduction in rates available for small business lending.
[20] *Id.*
[21] *Id.* § 4103(d)(1)(B), 124 Stat. at 2586.

In order to apply for a SBLFP loan, applicants must submit a small business lending plan, which will remain confidential, describing how its business strategy and operating goals address the needs of the small businesses it currently serves, along with a plan to provide marketing towards minority groups in their market in their language.[22] This ensures that the Treasury disburses the SBLFP money to organizations that not only have a strong business plan and that the money has an equally positive impact across all racial lines.

The second part of SBLFP is the State Small Business Credit Initiative ("SSBCI"). The SSBCI takes new federal funding and disburses it to states to use for their state capital access programs.[23] Capital access programs are a state's method of helping small business owners residing in the state to have the capital necessary to create and run a successful business.[24] The SSBCI allocates additional federal funding for states to use on their capital access programs which will assist a state-funded method of assistance for small and entrepreneurial businesses to get the capital necessary to succeed, which banks and other private institutions are not currently willing to provide.[25]

Entrepreneurs from the qualifying states will benefit by the additional capital made available to them. However, the method and criteria by which the funds are disbursed will continue to vary by state.[26] The federal funds will only be received by states which meet the following criteria: (1) The state's capital access programs must provide portfolio insurance for business loans based on a separate loan-loss reserve fund, (2) they must charge insurance premiums to the borrower and put the premiums into the reserve fund, (3) the state must deposit a sum of at least the quantity of insurance premiums paid by the borrower into the reserve fund, and (4) the state must only provide insurance for loans if the loan is for less than $5 million and if the borrower has 500 or fewer employees.[27] Under this program, the state will be able to receive up to the amount of insurance

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[22] *Id.* § 4103(d)(1)(E), 124 Stat. at 2587.
[23] *Id.* § 3303(a), 124 Stat. at 2570.
[24] *Illinois Capital Access Program*, IL. DEP'T OF COM. & ECON. OPPORTUNITY, http://www.commerce.state.il.us/dceo/Bureaus/Business_Development/Loan+Programs/cap.htm (last visited Mar. 30, 2011).
[25] Small Business Jobs and Credit Act of 2010 § 3303(a), 124 Stat. at 2570. State capital access programs provide basically the same service of making capital available to small businesses as the SBLF, but provide it through a state run, not federal organization.
[26] The Small Business Jobs and Credit Act simply gives federal funding to states for their capital access programs. It does not set out to manage how the state disburses the funds, as each individual state decides for themselves which firms have access to their own capital access programs.
[27] *Id.* § 3005(c)(4)(A), 124 Stat. at 2575.

premiums in its reserve fund paid by borrowers.[28] The state may use this money to contribute to the reserve fund, thereby freeing up additional money for lending.[29] The insurance premiums required for the loan are partially within the state's discretion.[30] The state may set their own rate as long as it is between two percent and seven percent of the total loan.[31]

To the credit of Congress, the Act is a relatively inexpensive way to get money into the hands of small business entrepreneurs, using an infrastructure that already exists. Borrowers will pay back the government and, since the federal discount rate is only .75%, the opportunity cost for the federal funds are very low.[32] However, the question still remains whether directly lending money to small businesses is the best way to improve their financial situation.

III. THE ACT'S EXPECTED BENEFITS TO ENTREPRENEURSHIP

The Small Business Jobs and Credit Act was passed specifically to address the economic problems faced by small business owners due to the recent financial crisis.[33] The recent economic crisis was basically caused by the overinvestment of banks, financial institutions and regular citizens' real estate mortgages, which ended up failing in great quantities. According to International Monetary Fund estimates, American financial institutions, like banks, who owned the mortgage backed securities, were forced to write off $1.5 trillion by the end of 2010.[34] Such a significant decrease in financial institutions' asset values sent many of them into insolvency.[35] Banks that were able to avoid bankruptcy became very conservative with their lending practices and effectively froze the credit market. Banks were faced with a shortage of cash and what little cash banks did have was often not being loaned out for fear of bank runs and for fear of the borrower not being worthy of credit in such difficult economic times.[36] The shortage of capital in banks extended to businesses and the impact was felt especially by small business owners and entrepreneurs, who

[28] *Id.* § 3005(c)(2), 124 Stat. at 2575.
[29] *Id.* § 3005(c)(1), 124 Stat. at 2575.
[30] *Id.* § 3005(e)(6), 124 Stat. at 2576.
[31] *Id.* § 3005(e)(5), 124 Stat. at 2576.
[32] *Federal Discount Rate*, BANKRATE (Mar 23. 2011), http://www.bankrate.com/rates/interest-rates/federal-discount-rate.aspx (last visited Mar. 30, 2011).
[33] Small Business Jobs and Credit Act of 2010 §4101, 124 Stat. 2582.
[34] Carter Dougherty, *I.M.F. Calls for Overhaul of Financial System*, N.Y. TIMES, Sept. 30, 2009, http://www.nytimes.com/2009/10/01/business/global/01imf.html.
[35] Robin Blackburn, *The Subprime Crisis*, NEW LEFT REV., Mar./Apr. 2008, at 50.
[36] David Weidner, *Why Banks (still) Aren't Lending*, MONEYCENTRAL (Mar. 3, 2011), http://articles.moneycentral.msn.com/Investing/Extra/why-banks-still-are-not-lending.aspx.

were victims of a 7.4% decrease in lending, the worst decrease since the Great Depression.[37] Banks were making very few loans, and the few loans they were making were not to higher risk firms like small or new businesses.[38] As a result, the economic climate for the small or entrepreneurial business owner has been extremely tough over the past two years. As the economic crisis has slowed, banks have slowly returned to lending. However, small businesses of America still remain under-capitalized compared to 2006 levels because of the lingering effects of the financial crisis.[39] The Act was passed by Congress to help relieve small business owners and entrepreneurs from their inability to receive credit by making credit available to them through the public sector, as well as create new tax benefits for struggling entrepreneurs.[40] The following outlines the Act from the listed perspective and analyzes its effect on small business owners and entrepreneurs.

A. *Availability of Capital*

The primary objective of the Act is to help struggling small businesses and entrepreneurs receive the access to capital that they are sorely lacking through a multitude of methods.[41] It addresses the problem through both direct and indirect means, and by using such a diverse approach, Congress hopes that the Act can catalyze the stagnant recovery of small businesses across the country. There is little doubt that small businesses will have access to much more capital as a result of this Act.

1. *Small Business Loans from the Small Business Lending Fund*

The largest single result of the Act is the creation of the $30 billion SBLFP.[42] The fund will distribute its funds to banks which apply and qualify for the loans. The qualifying institutions in turn receive a favorable interest rate for loaning the borrowed money to small businesses and entrepreneurs.[43] If the financial institutions borrow from the SBLFP and use the money properly by lending it to small businesses, they stand to make a greater profit than they could ordinarily achieve in the open market

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[37] Mark Whitehouse, *Loan Squeeze Thwarts Small Business Revival,* WALL ST. J., Mar. 15, 2010, at A20.
[38] Alexandra Cheney, *Lenders Stingy with Small Business Loans,* INC. (July 9, 2009), http://www.inc.com/news/articles/2009/07/loans.html.
[39] Conor Daugherty & Justin Lahart, *Recovery Gathers Steam,* WALL ST. J., Dec. 2, 2010, at A4.
[40] Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.
[41] *Id.*
[42] *Id.* § 4103, 124 Stat at 2585.
[43] *Id.* § 4103(d)(5)(A), 124 Stat. at 2589.

because of the governmental subsidy.[44] If the amount of small business loans as a percentage of total loans increases, the interest rate charged by the SBLFP significantly decreases, allowing a larger spread between the interest rate received and the interest rate owed to the extent previously described.[45]

There is no explicit requirement for financial institutions to use the SBLFP for small business loans; however there does not need to be. The interest rate incentive system, which was explained earlier, financially binds lenders to use the money to lend to small businesses to the best of their ability because of the substantial interest rate savings available to them. However, if firms neglect to use the SBLFP for its stated purpose, the federal government will profit greatly by charging a high interest rate to the negligent firm. By incentivizing small business loans, the SBLFP hopes that the $30 million fund will be lent to small businesses without having the oversight costs associated with requiring money to be spent a certain way.

2. *Tax Exclusion on Small Business Stock Gains*

The first method is a temporary 100% exclusion of capital gains on certain small business stock for non-corporate taxpayers as opposed to the typical fifty percent exclusion of the capital gain from qualified small business stock ("QSBS").[46] A QSBS is a C corporation that conducts an active trade or business and has gross assets of less than $50 million at the time the stock is issued.[47] A non-corporate taxpayer qualifies for this exclusion when it purchases a QSBS after the date of this law's enactment and before January 1, 2011, and holds the stock for five years.[48] The amount of capital gain that is excludable is the greater of (1) ten times the basis of the taxpayer's initial investment in the QSBS or (2) $10 million.[49]

This provision of the Act incentivizes individual investors to purchase QSBS. Investors purchasing the stock receive a significant tax benefit which can reduce their taxable income by $5 million for a $10 million investment, and reduce the investor's tax liability by $1.75 million if they are in the thirty-five percent tax bracket.[50] As a result, it would behoove

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44 *Id.*
45 *Id.*.
46 *Id* § 2011(a), 124 Stat. at 2554.
47 Stephen L. Feldman et al., *Small Business Jobs Act of 2010–Key Tax Incentive Provisions*, MORRISON & FOERSTER LLP, 1 (Sept. 28, 2010), http://www.mofo.com//files//uploads/images/100928-Jobs-Act.pdf.
48 *Id.*
49 *Id.*
50 These numbers were arrived at by my calculations of the result of the SBLF tax breaks on a hypothetical income level, investment, and tax bracket.

small business owners and entrepreneurs that qualify to distribute QSBS to issue and market additional stock because the Act makes it a very appealing investment for tax purposes until the incentive expires at the end of the year.

B. *Tax Benefits*

In addition to making capital available to small business owners through the SBLF and tax breaks for small business investors, Congress added provisions to the Act which give tax breaks directly to small businesses and entrepreneurs.[51] The benefits of these provisions are generally only available for a limited time, but certain business' strategy may be flexible enough to allow them to take advantage of such an opportunity.

1. *Reduction in Cost of Converting to an S Corporation*

The first example of a tax break created by the Act is the temporary reduction in the recognition period for the S corporation built-in gains tax.[52] The classification of a business as a C or S corporation has an impact on many aspects of its operations.[53] The primary difference between C and S corporations is the method of taxation.[54] The dividend income of a C corporation is taxed twice, once at the corporate level and once at the individual level as personal income.[55] S corporations, on the other hand, pay no corporate tax and all of the company profits are taxed as dividends, which can make S corporations more desirable than C corporations from a tax liability perspective to many small business owners.[56] However, one of the disadvantages of switching from a C corporation to an S corporation is the built-in gains tax.[57] The built-in gains tax requires newly converted S corporations to pay a thirty-five percent tax on gains that arose prior to the

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[51] Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.

[52] Feldman et al., *supra* note 47.

[53] *Sole Proprietorship vs. C Corporation vs. S Corporation vs. LLC*, THE MONEY ALERT, http://www.themoneyalert.com/Corp-Entity-Table.html (last visited Mar. 30, 2011).

[54] *Advantages of Corporations*, BUSINESSNAMEUSA.COM, http://www.businessnameusa.com/articles/corporation/C%20Corporation%20Benefits.htm (last visited Mar. 29, 2011).

[55] Aaron Larson, *The C Corporation*, EXPERTLAW (Dec. 2010), http://www.expertlaw.com/library/business/c_corporation.html.

[56] *S Corporation Facts*, NOLO (Jan. 2011), http://www.nolo.com/legal-encyclopedia/article-30002.html.

[57] Hart, King & Coldren Inc., *Converting From C Corporation to S Corporation*, FINDLAW (May 1, 2010), http://library.findlaw.com/2000/May/1/130239.html.

conversion to an S corporation, such as appreciated property, and is realized within ten years of the conversion.[58]

The Act shortens the ten year recognition period to five years for taxable years beginning in 2011, starting with the first day of the taxable year the election is in effect.[59] If the transition was made in 2009 or 2010, no built-in tax is imposed after seven years.[60] Also, beginning in 2011, no more built-in tax will be imposed on assets which have been held for at least five years since the transition from a C corporation to an S corporation.[61] Small business owners benefit from this tax break in that it provides a window of opportunity to convert from the C corporation to the more favorable tax scenario of the S corporation with a significantly lower transition cost. As an S corporation, the entrepreneur will usually have lower tax liability than a C corporation and thus allows more of the company's capital to be invested back into the company.

In addition to providing some tax relief to transitioning C corporations, the Act may create an opportune time in 2011 for shareholders of S corporations, in their recognition period, to sell assets which they have held for more than five years after their election to become an S corporation, thus avoiding the built-in gain tax.[62]

The Act certainly incentivizes switching from a C to an S corporation. However, switching is not always a good idea for all companies. One should only take advantage of this opportunity if it makes business sense. For example, while S corporations allow for only single taxation, increasing one's personal income is extremely costly under our current tax structure. Under an S corporation, all the income of the company is added to one's personal income and pushes them into a higher tax bracket, which can go as high as 38.6%.[63] With a C corporation, the first $50,000 is taxed at fifteen percent which will reduce the personal income of the owner and may allow them to be in a lower tax bracket with about the same level of actual income.[64] It is of the utmost importance that the tax consequence of such a change be considered before taking advantage of this provision.

Another issue with switching from a C to an S corporation is the availability of fringe benefits. C corporations allow employer-paid medical insurance, life insurance, disability benefits, death benefits, unemployment benefits, business expenses and employee wages to be deductable as

58 Feldman et al., *supra* note 47.

59 *Id.*

60 *Id.*

61 *Id.* at 2.

62 *Id.*

63 *Id.*

64 *Id.*

business expenses and excludable from the corporation's gross income for tax purposes, while an S corporation does not.[65] C corporations only have double taxation on profits disbursed through a dividend, which allows for some opportunities to avoid paying high levels of tax while still receiving the benefits of being a C corporation. In most cases, C corporation owners/operators may choose to structure their payment differently. Owners can receive their income as wages, consulting income, lease payments, interest payments or royalty payments as a way to avoid the double taxation of the C corporation. This provides substantial avenues of minimizing the tax consequences of the C corporation short of converting to an S corporation.

C corporations have another advantage in allowing for businesses to shift their income between years by adjusting the applicable tax year.[66] By law, individuals are required to base their fiscal year on the calendar year of January 1 to December 31.[67] S corporations generally follow a calendar year for their tax purposes and are required to have a § 444 election in order to do so because, unlike C corporations, they are not recognized as individual entities.[68] S corporations must adopt the fiscal year of its shareholders. C corporations on the other hand can pick the end of any month to conclude their fiscal year and their first fiscal year does not have to be twelve months long.[69] By designing the corporation's fiscal year to end a month earlier or later than December, small business owners may shift income between years. This is done through conveying an individual's personal tax income to the C corporation at the end of the corporation's fiscal year and then having it conveyed back to the person through some other form of payment outside of a dividend, like a lease payment.[70] This can be done indefinitely and ensure that the individual pays the lowest tax possible.[71]

It is absolutely necessary for the small business owner or entrepreneur to investigate all of the possible permutations involved in choosing whether to operate as a C or an S corporation. Even though the S corporation does not have double taxation, there are many ways shrewd and savvy individuals can avoid this pitfall. Generally, S corporations are much less versatile than the C corporations in terms of how to categorize income to its shareholders as payments other than wages to achieve a lower tax liability

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[65] *Id.* Owners of the business may deduct their salaries as executives and avoid paying corporate tax on them, which helps to minimize the tax liability difference between C and S corporations.
[66] *Id.*
[67] *Id.*
[68] I.R.C. § 444(d) (2006).
[69] *Advantages of Corporations*, *supra* note 54.
[70] *Id.*
[71] *Id.*

for the entrepreneurs. Typically, there is not a significant reason to switch from a C corporation unless the company is unable to structure payment to its shareholders in any other means than standard dividends to the level needed to avoid the penalty of double taxation; however, there are firms that fall into this category and the Act undoubtedly helps them individually and gives them a window of opportunity to convert at a lower cost.

2. *Extension of Tax Carrybacks*

The Act also extends the carryback of a small business's general business credit from one year to five years.[72] A carryback is a provision that allows a business to use a net-operating loss in one year to offset a profit in one or more previous years.[73] Extending the carryback allows struggling small businesses, which have suffered through the current financial crisis, to continue to reap the tax benefits of the carryback provision. The Act allows businesses with multiple years in a row of operating with a net-loss to actually receive tax refunds from the Federal Government instead of simply not paying any tax, thereby easing the financial strain on the business.[74] An eligible small business is defined in the Act as "a non-publicly traded corporation or partnership that has average annual gross receipts for the three taxable years prior to the current taxable year of $50 million or less" and is effective for credits determined in the taxpayer's first taxable year beginning after December 31, 2009.[75] Also, these credits may offset a qualified small business' alternative minimum tax liability, which typical small business tax credits do not.[76]

3. *Healthcare Deduction for the Self-Employed*

The Act also allows self-employed taxpayers to deduct the cost of obtaining health insurance for themselves, spouses, and children who have not reached the age of twenty-seven by the end of the taxable year for the computation of adjusted gross income, which is an above the line deduction.[77] For the purpose of the Healthcare Deduction provision, self-

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[72] Feldman et al., *supra* note 47.
[73] Definition of *Loss Carryback*, INVESTOPEDIA, http://www.investopedia.com/terms/l/losscarryback.asp (last visited Mar. 30, 2010).
[74] Feldman et al., *supra* note 47, at 2.
[75] *Id.*
[76] *Id.*
[77] *Small Business Jobs Act of 2010 Contains Important Tax Provisions—Year End Estate and Gift Tax Planning*, LOEB & LOEB LLP, 2 (Oct. 2010), http://www.loeb.com/files/Publication/a50afd1b-7450-4949-8593-4d74b59017 0d/Presentation/PublicationAttachment/49c73141-48c4-4cc0-8f1c-4ccd3dd60902/Tax%20Law%20Alert%2c%20Small%20Business%20Jobs%20Acts%20-%20October%202010.pdf.

employment includes individual practitioners as well as partners in partnerships.[78] The deduction is limited to the 2010 tax year only, making it of the utmost importance that small business owners and entrepreneurs act quickly in order to take advantage of the benefits created by the provision.[79] Congress wanted to help alleviate the double taxation self-employed individuals pay by shouldering both the "employer" and "employee" portion of the Federal Insurance Contributions Act ("FICA") tax.[80] For 2010, the rate is 12.4% of the first $106,800 of net earnings from self-employment for the elderly, survivors and disability insurance and 2.9% of all net earnings from self-employment for the Medicare hospital insurance tax.[81] The cost of health insurance is not deductible for purposes of computing net-earnings from self-employment.[82]

The benefit of the Heathcare Deduction provision is that it will provide financial relief to the self-employed in the form of a healthcare deduction.[83] Congress declares the reason for the deduction is to alleviate double taxation faced by those that are self-employed.[84] However, the logic behind that purpose is not entirely sound. Employees and the self-employed alike face the same level of taxation because employers do not take the "employer" portion of the FICA tax out of their profits; they take it out of the employee's salary or pass it on to the consumer in the form of increased prices.[85] In effect, this provision provides an incentive to become self-employed or at least subsidizes those that are self-employed. The deduction, however, is only for the 2010 tax year,[86] effectively making the incentive relatively small so as to not significantly impact anyone's decision to start their own business and become self-employed in the long run. The effect of this provision is simply providing a tax break to self-employed individuals in a way that encourages the purchase of healthcare, which saves the American taxpayer money.

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[78] *Id.*
[79] *Id.*
[80] *Id.*
[81] *Id.*
[82] *Id.*
[83] *Id.*
[84] *Id.*
[85] Andrew Chamberlain, *Who Really Pays the Corporate Income Tax?*, TAX FOUND TAX POL'Y BLOG (May 4, 2006), http://www.taxfoundation.org/blog/show/1467.html ("The burden of the tax ultimately falls on people–the owners, customers, or workers of the corporation.").
[86] *Small Business Jobs Act of 2010 Contains Important Tax Provisions- Year End Estimate and Gift Tax Planning*, *supra* note 77, at 2.

C. *Encouraging Small Business and Entrepreneurship*

The Act also has a few provisions dedicated to incentivize small business growth and investment as well as to promote entrepreneurship. The Act does this in a multitude of ways, primarily by temporarily expanding the scope of currently existing benefits.

1. *Expansion of I.R.C. § 179*

The first example is the expansion of § 179 in the Internal Revenue Code. Under the Code, taxpayers may typically deduct the expense of "qualifying property," as opposed to waiting to collect the money through yearly depreciation.[87] The maximum cost deduction is typically $250,000 of the cost of the qualifying property in the first taxable year the property is in operation and $25,000 in any following years.[88]

The Act however expands § 179 until the end of 2012 to allow an immediate deduction of $500,000 instead of $250,000 as the Code typically allows.[89] The Act also expands the definition of "qualifying property" to include certain types of real property, such as qualified leasehold improvement property, qualified restaurant property and qualified retail improvement property.[90] Congress' expansion of § 179 should provide liquidity relief to small businesses by allowing them to keep more of their money up front, as opposed to waiting to deduct the depreciation expense every year. The time value of money indicates that money in one's possession now is more valuable than that same amount of money later because of the ability to gain interest on money that is in one's control.[91] Allowing this deduction immediately, Congress is essentially giving the taxpayer more money at an earlier date than usual, which is beneficial to firms struggling with financial and liquidity problems.

The expansion of § 179 was also designed to promote entrepreneurship by expanding the type of property eligible for the deduction to include real property.[92] An entrepreneur looking to start a new business which requires real estate would benefit greatly from this provision. Allowing the immediate expensing of the real property up to $500,000 puts significantly more cash into the entrepreneur's hand which can allow them to borrow

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[87] I.R.C. § 179(a) (2006).
[88] I.R.C. § 179(b)(1) (2006).
[89] Feldman et al., *supra* note 47, at 3.
[90] 12 U.S.C.A. § 1245(a)(3) (West 2011).
[91] Definition of *Time Value of Money*, INVESTOPEDIA, http://www.investopedia.com/terms/t/timevalueofmoney.asp (last visited Mar. 29, 2011).
[92] Feldman et al., *supra* note 47, at 2.

less as well as ease the liquidity constraint, which causes so many new businesses to fail.

2. *Start-up Expenditures Deduction Increased*

Typically, entrepreneurs may deduct up to $5000 of start-up business expenditures in the taxable year the business begins. However, the $5000 deduction is reduced dollar-for-dollar by the amount the total business start-up expense exceeds $50,000.[93] Generally, start-up expenditures include costs paid or incurred in connection with "investigating the creation or acquisition of an active trade or business, creating an active trade or business, or certain activity engaged in for profit and for the production of income before the day on which the active trade or business begins."[94]

The Act extends this provision to allow entrepreneurs to deduct up to $10,000 of their start-up business expenditures and increases the $50,000 expenditure ceiling up to $60,000.[95] These changes go into effect beginning with the 2010 tax year.[96]

The initial cost of starting a new business is considerably less as a result of this provision of the Act. An entrepreneur's tax liability is reduced by an additional $3500 for start-ups in the thirty–five percent tax bracket and they can also spend an extra $10,000 on start-up expenses without losing their marginal tax benefits.[97] As a result, the company may use the extra tax savings on anything the business requires because it is cash that they no longer have to pay instead of a tax return that they will have to wait until the end of the year to realize.

IV. THE ACT'S SHORTCOMINGS

Despite all of the proposed benefits to small businesses and entrepreneurs, the Act is still very controversial in terms of its micro and macroeconomic benefit. Many believe that, while the Act has the correct intentions, it is not strong enough, nor properly directed to actually have a significant effect on small businesses and the economy in general. The Act falls short because it attempts to solve a multifaceted problem by only addressing one of the issues in a manner that itself is not free from controversy. The Act is tardy and redundant relative to other financial

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[93] *Id.* at 3.
[94] *Id.* at 3–4.
[95] *Id.* at 4.
[96] *Id.*
[97] These figures are based on the author's calculations of a hypothetical entrepreneur in a thirty five percent tax bracket.

crisis legislation, such as TARP,[98] and the methods used are not strong enough to invoke any real change in the economic standing of small businesses.

A. *Supply-Side Efforts Will Not Significantly Increase Lending*

The primary criticism of the Act is that the measures taken to create credit for small businesses will not have the desired effect because of the market's lack of demand for the small businesses' goods.[99] Economic theory is based on the relationship between supply and demand, and changes in each have significant effects on the economic system. A decrease in the quantity produced in the economy can be attributable to either a decrease in the supply or demand of a particular good. The Act addresses the credit crunch facing small businesses as a supply problem and attempts to fix it by making $30 billion in low-cost capital available to small businesses through the SBLF.[100] Critics argue this is not the solution to the problem and cite the failure of TARP's Capital Purchase Program ("CPP") to create jobs or improve small business' access to credit.[101] The CPP provided hundreds of billions of dollars, as opposed to the SBLFP's $30 billion, to banks specifically for small business lending; however, most recipient banks decreased their lending after receiving the money.[102] The CPP did restore liquidity to banks, but because very few small business loans are securitized, there was very little impact on small business lending.[103] Even if there were figures which show a correlation between an increase in small business loans and the operation of TARP, critics would argue that the TARP money did not increase small business lending because it simply crowded out private lending and, in effect, actually damages the economy.[104]

The Congressional Oversight Panel attributes TARP's failure to increase small business lending to the lack of demand for credit for small businesses.[105] In the fourth quarter of 2008, net 57.7% of the respondents to the Federal Reserve Board's Survey of Senior Loan Officers reported that demand had fallen for small business loans–a figure that rose to 63.5%

[98] Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 2, 122 Stat. 3765.
[99] H.R. REP. NO. 111-499, at 3 (2010).
[100] *Id.* at 9.
[101] 111TH CONG. OVERSIGHT PANEL, SMALL BUSINESS JOBS ACT OF 2010, at 4 (2010).
[102] *Id.*
[103] *Id.*
[104] 156 CONG. REC. H4449 (June 15, 2010) (statement of Rep. McClintock).
[105] *See* 111TH CONG. OVERSIGHT PANEL, *supra* note 101, at 4.

the following quarter.[106] Even now, 9.3% of survey respondents continue to report falling demand, suggesting that some of the reduction in small business lending may be in fact the result of a lack of demand.[107]

Critics argue the lack of demand could be due to the fact that there are a limited number of creditworthy small businesses that are seeking loans due to last year's economic crisis as well as the financial uncertainty the U.S. is facing today.[108] They believe a better solution would involve getting creative in finding ways to stimulate small businesses from the demand side as opposed to "pushing on a string" by increasing the supply of available credit when there is not sufficient demand to warrant it.[109] If a lack of sales is what is really hurting small businesses, the lion share of the Act does not significantly address that problem.[110] Regardless of the effectiveness of the Act on the economy as a whole, entrepreneurs and investors alike should take advantage of the tax benefits or incentives that the Act creates.

B. *Poor Timing*

While increasing the amount of lendable funds available to small business owners and entrepreneurs is a good thing for the small business owners, the timing of the SBLFP creates some issues that could make the Act ineffective and detrimental to the economy. The general consensus is that the economy has bottomed out and has been gradually building a recovery since early 2010. Almost a full year after economic recovery began the need to help small firms receive access to credit seems to be diminishing quickly.[111] The Act simply may be too late to really have any significant impact on assisting small businesses. There may be not enough small businesses that are credit constricted to incentivize lending institutions to take on the SBLFP loans because the market for small business loans is weak and participating institutions will not be able to get a significant increase in their small business loans, which would cause the interest rate on their loan to be relatively expensive. If the lending institutions do not have an incentive to engage in the SBLFP, the $30 billion set aside for the program will remain largely inactive and not have

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106 *Id.* at 5.
107 *Id.*
108 *Id.*
109 *Id.*
110 The biggest portion of the Small Business Jobs and Credit Act is the creation of the Small Business Lending Fund which makes capital available to small businesses who need it. If the critics are correct that there is plenty of capital, just no demand for small businesses' products, then the bill is not directly addressing the real problem facing small businesses.
111 Philip Newswanger, *Nice bill, bad time, says one critic,* INSIDE BUS. (Oct. 1, 2010), http://www.insidebiz.com/news/nice-bill-bad-timing-says-one-critic.

the effect of helping small business owners and entrepreneurs as Congress desired.

C. *The Scope of the Bill is Too Limited*

The Act also has too short of an operation to really make a significant difference. There is essentially a one year window for lending institutions to receive loans from the Small Business Lending Fund.[112] Also, the financial incentive for making small business loans is only for a two-year period.[113] The incentive period, where making loans to small businesses is incentivized, only lasts for two years past that period.[114] That means the loan only has a financial incentive for up to four years of a ten-year loan, which is not substantial.

The tax benefit provisions that involve planning are not given a long enough window of operation to allow businesses to reap the available benefits.[115] For example, the Act creates a built-in gain tax exemption for companies looking to switch from a C Corporation to an S Corporation, a conversion that typically lowers a business' tax liability due to the avoidance of double taxation.[116] Critics feel this exemption is a good idea, however the window of opportunity for making the decision to convert is too small compared to the extent of the benefits made available to significantly impact most business owners' decision to convert from a C Corporation to a S Corporation.[117]

Another provision with too limited a window is the 100% tax exemption of capital gains associated with the ownership of QSBS for a period of at least five years.[118] In order to be eligible for the tax exemption, the stock must be purchased between the passage of this law and January 1, 2011, which was only a three-month window, and has already passed.[119] While the exemption does make owning stock in small businesses very appealing from a tax perspective, three months is simply not enough time to secure any significant amount of investors and is simply not an actionable tax policy.[120] Small business owners will struggle to even decide if issuing

[112] Small Business Jobs and Credit Act of 2010 § 4109(a), 124 Stat. at 2589.
[113] *Id.* § 4103(d)(5)(A)(iii), 124 Stat. at 2583.
[114] *Id.*
[115] Newswanger, *supra* note 111.
[116] Feldman et al., *supra* note 47.
[117] *Id.*
[118] Small Business Jobs and Credit Act of 2010 § 2011.
[119] *Id.*
[120] *Lipservice (Bipartisan Pro-Growth Tax Policy Demagoguery)*, VENTURE POPULIST (Nov. 17, 2010), http://venturepopulist.com/2010/11/lipservice-bipartisan-pro-growth-tax-policy-demagoguery/.

stock is the proper financing strategy in a three month period, which does not even take into account the time needed for marketing as well as the time the buyer will desire to conduct due diligence on the company. The tax exempt capital gain of small business stock is a very desirable incentive for investing in small business, however three months is simply not enough time to create a large influx of investment into these credit constrained small businesses.[121]

The Act has also been called too limited in that it does nothing to help small businesses by attempting to stimulate demand for their products.[122] The Act does a lot to give small businesses and entrepreneurs the capital necessary to run their business but does nothing to give them a market in which to sell their goods. Possible improvements suggested by small business advocates would be to require the federal government to give a certain percentage of their contracts to small businesses and give tax benefits to those companies that choose to do business with small businesses.[123] This would provide more opportunities for small businesses to sell their goods, which many believe is the largest problem small businesses face today.

D. *Unforeseen Consequences*

Another way this Act could hurt entrepreneurs is through the legal loophole it creates in § 1341, where it gives the Administrator of the Small Business Administration ("SBA") the power to, "promulgate regulations to provide adequate protections to individuals and business concerns from liability under this subsection in cases of unintentional errors, technical malfunctions, and other similar situations."[124] Some experts, including the Administrator of the SBA, fear that this creates a loophole that allows large firms to avoid liability for contracting fraud, which could have an overall negative impact on the credit market and would make it harder for small business owners and entrepreneurs to get loans at low interest rates.[125] It also could effectively repeal the Small Business Act requiring twenty–three

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[121] Feldman et al., *supra* note 47.
[122] *Squawk Box: Huge Loophole in Senate Jobs Bill* (CNBC television broadcast Sept. 14, 2010), *available at* http://www.youtube.com/watch?v=SQcUa2wb5hY&feature=related [hereinafter Lloyd Chapman Interview] (interviewing Lloyd Chapman, President and Founder of the American Small Business League).
[123] *See id.*
[124] Manikandan Raman, *Jobs Bill Passed, But Loopholes Remain*, INT'L BUS. TIMES, Sept. 24, 2010, http://www.ibtimes.com/articles/65462/20100924/jobs-bill-us-obama-small-business-sba-house-deficit-small-banks-economy-asbl-lockheed-martin-boeing.htm; *see* Small Business Jobs and Credit Act of 2010 § 1341(w)(4), 124 Stat. at 2537.
[125] Raman, *supra* note 124.

percent of government contracts to go to small businesses and allow large Fortune 500 companies to dominate the market for public sector contracts in a way not allowed before.[126]

Another problem is that it deals only with the credit problem small business owners and entrepreneurs face, but does not even begin to address the shortage of demand that businesses are facing.[127] Additional capital is great for helping companies grow or expand, however if there is not enough demand for their products, the expansion will only increase their overhead without actually increasing their profits, thus dooming the small business to fail. The bill can be viewed as making money appear cheap to small business owners who will borrow and get in over their heads, and ultimately default. Critics argue that this bill helps venture capitalists greatly by providing lots of tax loopholes for investment in small businesses, however it does not really address the true reason small businesses are failing—a lack of sales.[128]

V. COMPARISON OF THE SMALL BUSINESS JOBS AND CREDIT ACT TO TARP

The Act's primary function is the creation of the Small Business Lending Fund Program. The SBLFP takes public money and makes it available to financial intermediaries who then receive financial incentive to lend that money to credit constrained small businesses.[129] There have been a few pieces of similar legislation recently passed to provide economic relief to American businesses in the past year's financial crisis, namely, TARP and various other SBA initiatives. The largest example of governmental TARP which was designed to "provide authority for the federal government to purchase and insure certain types of troubled assets for the purposes of providing stability to and preventing disruption in the economy and financial system and protecting taxpayers . . . ."[130] Put more simply, TARP was designed to relieve lending institutions of their illiquid assets and replace them with cash to help facilitate lending. The Act has been compared to TARP, and a good way to understand how the new bill will operate is to look at how similar bills enacted in the past have operated.

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[126] Lloyd Chapman Interview, *supra* note 122.
[127] *Id.*
[128] *Id.*
[129] Small Business Jobs and Credit Act of 2010 § 1403(b)(1), 124 Stat. at 2585.
[130] Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 2, 122 Stat. 3765, 3765.

TARP was created rather quickly after the financial crisis to prevent liquidity lacking financial institutions from failing.[131] The purpose of TARP was to purchase troubled assets from banks in order to give banks cash and liquidity while removing the risk associated with owning troubled securities. The general consensus is that TARP was successful in stabilizing the economy, helping to avoid a financial meltdown of a magnitude not seen since the Great Depression; however it seems to have failed in meeting its secondary goals of reducing unemployment, reducing the number of foreclosures, and easing credit constraints on small businesses.[132]

To deal with this problem, Congress passed the Act which created the SBLFP, which makes capital available to certain financial institutions in the form of a simple incentivized loan.[133] Many critics feel this is simply "TARP Jr.," and is simply extending the benefits of TARP past its October deadline. The Special Investigator General of TARP, Neil Barofsky, said that "in terms of its basic design, its participants, its application process, and perhaps its funding source from perhaps an oversight perspective, the Small Business Lending Fund would essentially be an extension of TARP's Capital Purchase Program."[134] As a result, there is no need for this redundant legislation because the problem of small business lending is being addressed already, and if the means in which TARP is addressing the problem is ineffective, then there is no reason to invest further in the same method.[135] Many committee Republicans do not feel the answer to small business owners and entrepreneur's woes is taxpayer-funded bailouts, however little argument can be made that making this money available to small business owners and entrepreneurs is not beneficial from the perspective of the small business owner, even if its cost to taxpayers exceeds its benefit.

Many of the criticisms of TARP do apply to the Small Business Jobs and Credit Act. If small business loans are not occurring because of a lack of demand by small businesses, this legislation does nothing to help. As stated before, many critics argue a lack of sales, not credit, is the problem facing small businesses today.[136] The Act's similar supply side attempt to increase lending to small businesses as TARP will prove ineffective if a

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[131] The economic crisis began in 2007, however it was not recognized as a serious issue that would require governmental inference until only a few months before TARP was passed in October 2008.

[132] *TARP: Government Bailout Failed in Many Ways, Says Watchdog,* ABCNEWS (Jan. 31, 2010), http://abcnews.go.com/Business/tarp-government-bailout-failed-reduce-foreclosures-unemployment-watchdog/story?id=9702600&page=3.

[133] Small Business Jobs and Credit Act of 2010 § 4103, 124 Stat. 2504.

[134] 156 CONG. REC. H4449 (June 15, 2010) (statement of Rep. McClintock).

[135] *Id.*

[136] Lloyd Chapman Interview, *supra* note 122.

lack of sales is in fact the cause of small businesses' suffering. However, TARP was highly successful for its basic purpose of stabilizing the financial market and any further symptoms addressed but unfinished by TARP will be eased with the Act.[137]

In many ways, the Small Business Credit and Jobs Act is similar to TARP. In the Act, there is not a complex transaction and exchange of illiquid assets for cash as there was in TARP.[138] There will be no governmental ownership of private assets under this law. The Act creates the SBLFP, which is similar to TARP's Capital Purchase Program, albeit on a much smaller scale.[139] However, the Act does a lot of other things, as was stated previously in the explanation of the bill. For example, it creates tax exemptions for small business investors and allows a tax reduction for small businesses that wish to change to a tax-favorable S Corporation.[140] All of these additions should be helpful to loosen the noose around small businesses.

Also, a significant portion of TARP was designed to assist large financial institutions who had liquidity issues due to the bad mortgage assets on their books, which limited their ability to give loans at all, much less to a risk-taking small businesses. One of the major criticisms of TARP is that it bails out the holding companies, not the individual banks that do the lending.[141] As a result, the holding companies can use the TARP money for a wider variety of activities besides lending.[142] Unlike TARP, the Act's SBLFP is only available to smaller financial lending institutions, not holding companies. Also, the firms are incentivized to make loans to small businesses through interest rate manipulation which did not exist under the TARP program.[143] The Act is more precisely targeted than TARP, which generally threw large sums of money at holding companies, hoping they would spend the money on loans. The SBLFP is required to lend only to smaller institutions, large holding companies are not allowed to

[137] John C. Coates & David S. Scharfstein, Op-Ed., *The Bailout is Robbing Banks*, N.Y. TIMES, Feb. 17, 2009, at A27.
[138] In addition to supplying credit to businesses like the Small Business Jobs and Credit Act, TARP also created another significant event that the Small Business Jobs and Credit Act does not when it purchased toxic mortgage-backed securities from companies.
[139] TARP loaned out $247 billion to floundering businesses while the Small Business Jobs and Credit Act provides for a maximum of thirty billion loaned to small business owners and entrepreneurs. Small Business Jobs and Credit Act of 2010 § 4103(a)(2), 124 Stat. at 2585.
[140] H.R. REP. NO. 111-499, at 5 (2010).
[141] Coates & Scharfstein, *supra* note 137.
[142] *Id.*
[143] H.R. REP. NO. 111-499, at 5.

participate.[144] Congress has a narrower focus in this bill than the general bailout plan of TARP.

The Act could be less effective than TARP due to the different time period it was passed in. Banks are not on the verge of collapse and the Act is designed to benefit small business owners and entrepreneurs, not banks. The hope of Congress is that the financial institutions will see the opportunity for profit the Act provides and apply to be a part of the program.

However programs which put other parties between the government and the party it is designed to help can sometimes be ineffective due to unforeseen lack of cooperation by the third parties or a misaligning of interests. If the incentives are not significant enough, the funds may never reach the entrepreneurs because in order for them to do so, financial institutions must apply for the program. TARP was initially designed to prevent economic collapse and help failing banks by buying up their illiquid assets. This was later abandoned; however, the Treasury did purchase preferred stock to directly infuse the troubled businesses with capital.[145] It also had the secondary goals of helping ease the credit crunch on small businesses across the nation and reduce unemployment, which it was not successful in doing.[146] A reason the secondary goals were not met was because the interest of large financial holding companies and that of the federal government did not align. The holding companies want to make the most profit they can for their shareholders and will use any capital they have to do so. The government wanted these firms to use the borrowed TARP funds to make loans, which did not occur to the level desired by legislators. A similar problem could occur in the Act, however it is much less likely to due to the financial incentives put in place by the Act which makes loaning to small businesses more profitable to the lender due to a larger spread in interest rates.

VI. OPERATION WITH CURRENT ECONOMIC FORECAST

The success of the Act largely depends on how the economy progresses over the next year. As stated earlier, the key issue with the Act is whether the increased amount of capital made available to small business owners and entrepreneurs through the bill adequately addresses the problems that small businesses are actually struggling to confront. If the problem is the lingering effects of the credit crunch, the Act should do a lot to help small businesses. However, if small businesses are actually primarily struggling with a lack of sales, as many small business interest groups like the

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[144] *Id.* at 10.
[145] *See* 12 U.S.C.A. § 5211 (West 2010).
[146] W.W., *supra* note 5.

National Federation of Individual Businesses suggests,[147] then Congress' efforts with the Act will simply be "pushing on a string."[148] On the other hand, even if the efforts of Congress were in fact misguided, that does not mean the Act will not be successful in helping small businesses. The success of the bill will depend on the future economic climate. If the economy stays poor or gets worse, it is safe to say that demand for goods will not increase and small businesses will continue to struggle selling their products and no amount of capital made available will be able to help. However, if the economy begins to recover and demand increases, small businesses will be able to increase production to keep up with the increase in demand. In that case, the Act could play a vital role in ensuring the lingering effects of the credit crunch do not prevent small businesses from being able to rise up to meet the demand and begin to drive the economy forward toward recovery.

The current economic outlook is generally one of cautionary optimism.[149] According to Ben Bernanke, the Chairman of the Federal Reserve, "Things have stopped getting worse . . . They're getting a little better."[150] This forecast is promising when paired with the Act taking effect because both the supply of credit and demand for their goods should be increasing in the next year when the economy recovers and they will be fully capitalized and ready to meet the market's increase in demand when more cautious and pessimistic business owners will not be.[151]

Despite this message of optimism, the possibility of economic stagnation still exists. Many experts and business officials believe there will be a "double-dip" recession.[152] Economist Robert Shiller believes the uncertainty felt by economic actors as a result of the immense governmental bailout programs makes them apprehensive of making

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[147] Press Release, Brad Close, VP of Federal Public Policy at the National Federation of Independent Business, Small Business Lending Fund Act and Small Business Jobs Tax Relief Act (June 18, 2010), *available at* http://www.nfib.com/press-media/press-media-item?cmsid=51822.

[148] 156 CONG. REC. H4449 (June 15, 2010) (statement of Rep. McClintock).

[149] Kent Hoover, *Small business lending 'starting to turn,'* ABJ ENTREPRENEUR (Jan. 21, 2011, 2:27 PM), http://www.abjentrepreneur.com/news/2011/01/sba-lending-starting-to-turn-issues.html.

[150] *Id.*

[151] The Small Business Jobs and Credit Act makes credit available to small businesses while the increase in economic activity promised by the favorable economic forecast will increase demand for their products and create a flow of capital and products through small businesses. *See* Small Business Jobs and Credit Act of 2010, Pub. L. No. 111-240, 124 Stat. 2504.

[152] Simon Constable, *Economist Shiller Sees Potential for 'Double Dip' Recession*, WALL ST. J., Aug. 28, 2010, http://online.wsj.com/article/SB10001424052748704147804575455370525902224.html.

positive business transactions and will lead to another economic downturn.[153] If this is in fact the case, the Act may be as ineffective at improving unemployment and stimulating small business growth as TARP because making additional credit available to businesses does nothing if there is no profitable activity the businesses can put the capital towards.

Another issue is whether banks and other lending institutions will apply for the SBLFP. The first term sheets were given out in December and there are no projections for how many banks will tap this resource.[154] Applications are due March 31, 2011.[155] It is very important for the success of the Act that banks and lending institutions apply for loan money because even though the bill promises $30 billion of capital to small businesses, the bill is structured to only provide as much capital as banks are willing to sign up for and loan out. If the number of banks that sign up for the SBLFP is high, there will be a lot of additional credit for small businesses and entrepreneurs. If it is low, then the bill will be largely ineffective.

The concern with banks not significantly participating in the program is a real one. "Under the program, banks with assets of $10 billion or less can access capital from the Treasury Department at an initial dividend rate of five percent. If a bank increases its small business lending, the dividend rate will fall to as low as one percent. But if a bank fails to increase its small business lending, the dividend rate will increase to seven percent or more."[156] If there is not enough demand for loans, as many critics believe to be true, this could prove to be an expensive source of capital for these lending institutions and banks may not want to participate in the program because of the aforementioned risk. For example, as of January 14, 2011, only one of Alabama's 140 banks that are eligible for the SBLFP has applied for it.[157]

Despite reservations the general consensus seems to be optimistic.[158] Paul Merski, the Senior Vice President and chief economist at the Independent Community Bankers of America, believes, "We're going to see a lot of applications."[159] Unfortunately there are no figures available for

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[153] *Id.*
[154] Hoover, *supra* note 149.
[155] *Id.*
[156] *Id.*
[157] *Id.*
[158] Experts' opinions seem to be split, there is one negative outlook for just about every positive one. However general consensus cannot rely on the opinions of the media. The general opinions of people in charge of running the economy, such as the Chairman of the Federal Reserve Ben Bernanke and Secretary of the Treasury Tim Geithner are a better indicator of the current economic outlook. Both of the previously mentioned men believe the worst is over and the economy is in a period of gradual recovery.
[159] Hoover, *supra* note 149.

the quantity of lending institutions that have or will apply to be a part of the SBLFP and no one really knows for sure how much capital is going to be made available to small businesses through the SBLFP next year.

VII. CONCLUSION

The Act is a complex and comprehensive law designed to help struggling small businesses and entrepreneurs receive the capital and liquidity necessary to succeed and no longer be stifled by the lingering effects of the recent financial crisis. Congress set aside an additional $30 billion to be loaned to small businesses as well as create new and expand old tax benefits to small businesses.[160] The Act creates a temporary tax exemption for investments in QSBS as well as reduced tax periods for the built-in tax for converting to a typically tax favorable S Corporation.[161] Congress is hoping these measures will give small business owners and entrepreneurs the capital they need to run a successful business. However, despite Congress' best efforts, in the end, this law will be ineffective.

The first reason is that the Act is misguided and insufficient to create any real benefit is that the Act does nothing to deal with the demand side of the business. Small business owners are in many situations unwilling to take financial risks, not because of a lack of available credit, but a fear that there is not enough demand for their products to support the additional investment.[162] As long as consumers are concerned about healthcare and unemployment, they will not have the confidence to spend like they did before the financial crisis, which makes the marketplace less appealing for business.

Also, the provisions and measures that the law does take are good ideas; however, the window or extent of which the measures are taken are simply not sufficient to create a significant benefit to small businesses or entrepreneurs. The timing of the bill is not great and the time windows for receiving certain benefits are too small and limited for many businesses to take advantage of. An example is the built-in tax period reduction. It will be a great help to businesses, but the window for action is so small that a business is very unlikely to be able to make a good decision, so the tax incentive is in some ways, inoperable.[163]

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[160] H.R. REP. NO. 111-499, at 3 (2010).
[161] *Id.* at 5.
[162] Press Release, Printing Industries of America, New Law Extends Investment Incentives for 2010: More Certainty is Needed (Sept. 27, 2010), *available at* http://www.printing.org/news/6545.
[163] Feldman et al., *supra* note 47.

This Act has also been compared heavily to TARP and called by some simply a temporary extension of TARP.[164] The SBLFP is very similar to the Capital Purchase Program of TARP in that is simply increases the supply of credit available to small businesses by making a slush fund available to lending institutions who may chose to lend it to small businesses in order to receive a favorable interest rate. The Act may differ in a few key ways in that it is much more focused on improving credit availability to small businesses while that was only a secondary concern for TARP, which was primarily concerned with stabilizing the economy.[165] It also has numerous tax benefits for both small business owners and small business investors. However the primary part of the Act is the creation of the SBLFP, which operates almost identically to TARP. If history is any indication, the Act will fail to improve the financial health of small businesses just as TARP did.

The Act attempts to walk a fine line between offering comprehensive benefits to business without being too costly to the taxpayer. It would behoove businesses to become aware and familiar with the provisions of this law because there are considerable opportunities to have thousands of dollars in tax savings if one is able to act quickly because the window of opportunity in the Act is very small. However, on the macroeconomic level, the Act will not have the effect Congress desired because it is addressing only one of the many problems small businesses are facing in today's economic climate. The Act does not help ease the uncertainty in the economy or attempt to increase consumer demand for small business' products.

In the end, the success of the Act will depend on the state of the American economy over the next year. If the economy improves and consumer demand increases, the credit made available to small businesses by the Act will allow entrepreneurs to act more quickly than under normal market conditions due to the increased supply and lower cost of credit. However, if the economy remains stagnant, the Act will simply be pushing on a string, unable to create any real change in the economic climate small businesses operate in. Individual small businesses may feel some relief as a result of the Act in the form of tax benefits and some extra available credit; however the results will be largely superficial. Unfortunately, the Act is more like an aspirin to relieve the pain felt by small businesses today rather than an antidote.

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[164] 156 CONG. REC. H4449 (June 15, 2010) (statement of Rep. McClintock).

[165] Ben S. Bernanke, Chairman, Fed. Reserve, Speech at the Nat'l Ass'n for Bus. Econ. 50th Annual Meeting (Oct. 7, 2008), *available at* http://www.federalreserve.gov/newsevents/speech/bernanke20081007a.htm.